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ABSTRACT

This report presents the results of various California community college financial audits and reviews for fiscal year (FY) 1987-88. Section I explains the scope, purpose, and procedures of annual financial audits, which are conducted to evaluate financial statements, encourage sound fiscal management practices, ensure proper use of public funds, and strengthen fiscal accountability at the district level. This section includes an analysis of the 495 citings contained in the FY 1987-88 audit. Section II reports on the design and implementation of a comprehensive system for monitoring and evaluating the financial condition of community college districts. Section III presents results of audits of district attendance accounting and reporting procedures, completed to ensure compliance with state reporting regulations for attendance and apprenticeships. Section IV focuses on audits of the district use of federal vocational education funds and compliance with relevant regulations. A concluding section comments on each type of fiscal or compliance review, and briefly discusses plans of the Chancellor's Office that may affect community college fiscal and compliance accountability in coming years. Appendixes contain "Community Colleges State Compliance Requirements, 1987-88 Fiscal Year Audits," "Annual Audit Report Reviews and Citing Resolution Procedures," and "Office of Management and Budget, Circular A-133: Audits of Institutions of Higher Education and Nonprofit Organizations." (JMC)

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Report on Fiscal and Compliance Accountability

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Report 89-1

Fiscal Services/Fiscal and Program Standards Accountability
Chancellor's Office
California Community Colleges
Sacramento, California

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Executive Summary

Section 70901 of the *Education Code* vests the Chancellor's Office with responsibility for providing leadership and direction in the development of the California Community Colleges as an essential component of the State's system of public higher education. To that end, the Chancellor's Office oversees community college programs and advises and assists local governing boards in interpreting and implementing State and federal laws affecting community colleges. An important part of that oversight function is the fiscal and compliance accountability activities summarized in this report.

The annual financial and compliance audits conducted in each district by private accounting firms pursuant to the *Education Code* (Section 84040) attest to the accuracy and completeness of district financial statements. The Chancellor's Office oversees these contracted district audits (CDA) in cooperation with the State Department of Finance and, in accordance with the *Code* (Section 84040.6), presents this summary report of the results of the CDA reports for Fiscal Year 1987-88.

Other fiscal and compliance accountability efforts are jointly administered with the Department of Finance. The *Education Code* (Section 84040.5) authorizes the Department of Finance to conduct compliance reviews of community college apportionment reports as part of its responsibility to encourage sound fiscal administration of State funds. Once the reviews are completed, the Chancellor's Office works with the districts to correct attendance reporting practices and, when appropriate or necessary, adjust the amount of State General Apportionment or categorical funds a district receives.

Independently, the Chancellor's Office has responsibility for monitoring the fiscal condition of community college districts (Chapter 1486, Statutes of 1986). The office also conducts financial and compliance reviews of federally funded vocational education programs to ensure that districts comply fully with the Carl D. Perkins Vocational Education Act of 1984, Public Law 98-524.

Beyond presenting an overview of these activities, this report identifies developments that may influence community college fiscal accountability in the future. Because of the pervasive effects that fiscal and compliance accountability often have on college operations and programs, greater monitoring efforts may be needed in response to current and future community college reform. Reporting requirements created by implementation of proposed new federal regulations for higher education audits, program-based funding, and the statewide Management Information System will require the Chancellor's Office to work more closely with district personnel and contract auditors.

Introduction

This report presents the results of various community college financial audits and reviews for the 1987-88 fiscal year and a summary of contracted district audits, as required by Section 84040.7 of the *Education Code*. It also explains the role of the Chancellor's Office in encouraging and guiding accountability efforts at the district level. A concluding section comments on each type of fiscal or compliance review, and briefly discusses plans of the Chancellor's Office that may affect community college fiscal and compliance accountability in coming years.

Community college districts are complex organizations; they consist of many programs and activities, each with its own assigned area of responsibility. One of the many activities under the control of local administrators is the financial management of a district. District financial accountability is maintained primarily through contracted district audits (CDAs) conducted by private accounting firms hired by the district. As discussed in greater detail in Section I, these audits evaluate district financial statements and perform limited compliance reviews in areas not directly related to financial administration.

Local administrators also are responsible for maintaining the fiscal health of their districts. In recent years, some districts have experienced such severe financial problems that additional State aid has been required to save their educational programs. For that reason, the Chancellor's Office now operates a fiscal-stability monitoring system that provides early identification of and assistance to districts experiencing financial difficulties. This system, discussed in detail in Section II, is another accountability measure designed to strengthen district financial administration.

Student attendance audits constitute a major area of compliance accountability. Under current funding formulas, State General Apportionment revenue is determined to a large extent by the amount of time students spend in class, commonly known as Average Daily Attendance (ADA). Although local audits review ADA as it relates to district revenue, the Department of Finance has recognized that more detailed attendance audits (see Section III) are required to determine district compliance with legal provisions that control State funding. The Chancellor's Office is responsible for ensuring that districts correct reporting errors and change improper attendance procedures identified through such audits.

For similar reasons, the Chancellor's Office conducts detailed fiscal and compliance audits of vocational education programs, as described in Section IV. These reviews also are designed to determine district compliance with specific federal and State statutes and regulations to a greater degree than inspections performed during contracted district audits.

The concluding section of this report, "Looking to the Future," discusses factors that are expected to influence community colleges audits in the near future. It cites current changes in accountability procedures and reports on the status of other developments, such as program-based funding and the statewide Management Information System, that may well affect the way in which the fiscal management of California's community colleges is evaluated. Last year's report on fiscal accountability presented a detailed discussion of compliance reviews of Extended Opportunity Programs and Services. This year, because of increased staff efforts to assess the effects of community college reform legislation on existing accountability efforts and to coordinate financial and compliance audits, such specialized reviews have been curtailed temporarily.

I ▸ Annual Financial and Compliance Audits

By law, all community college districts are required to undergo annual financial audits conducted by certified public accountants or public accountants licensed by the State Board of Accountancy (Section 84040, *Education Code*). The purposes of these audits are to:

- Evaluate annual financial statements,
- Encourage sound fiscal management practices,
- Ensure proper use of public funds, and
- Strengthen fiscal accountability at the district level.

The Department of Finance prescribes the financial statements and other information to be included in the auditor's report, and in association with the Chancellor's Office, develops audit procedures for evaluating specific community college programs. For that purpose, the Department and the Chancellor's Office jointly issue an audit guide, *Standards and Procedures for Audits of California Community Colleges*.

The guide requires each auditor to review a district's financial statements and related fiscal operations. Because community college districts are governmental units, auditors also are required to review each district's compliance with laws and regulations affecting the receipt and expenditure of public funds in general. These evaluations culminate in contracted district audit reports that render opinions on the districts' financial statements and provide positive assurances regarding internal controls and compliance with selected State and federal statutes and regulations.

Although the guide stipulates areas to be examined and the format of the audit reports, community colleges districts are responsible for engaging independent accounting firms to perform annual audits in accordance with established guidelines.

Audits of community college districts have a different focus than those of public agencies and private business. In contrast to firms that derive income from the sales of goods and services, community college districts are funded on the basis of the number of students attending and the assessed valuation of property in the district. In addition, districts receive significant funding from specific categorical programs such as Extended Opportunity Programs and Services and Disabled Students Programs and Services, among others. They also receive federal funds under the Perkins Loan Program, Guaranteed-Student Loan Program, Job Training Partnership Act and the Carl D. Perkins Vocational Education Act. Each of these federal programs has statutory and regulatory requirements that control the receipt and expenditure of funds. Financial audits of community colleges are to encompass

all funds controlled by districts. Consequently, auditors review categorically funded programs to ensure equitable allocation and proper expenditure of the funds.

To assist district auditors in reviewing categorical programs, the annual audit guide includes procedures suggested in the federal *Compliance Supplement for Single Audits of State and Local Governments*. Additional assistance is provided to auditors in another section of the guide that presents State statutes and regulations for which compliance is a matter of concern. Accordingly, the Chancellor's Office creates State-compliance testing structures that include detailed descriptions of compliance requirements and suggested audit procedures. The auditors are required to review these compliance areas in every district as part of their annual examination. Compliance areas may be modified approximately every two years as areas of concern change. (The State-compliance testing structures for Fiscal Year 1987-88 are listed in Appendix A.)

After being approved by the local governing board, the completed district audit report is to be filed on or before November 15 of each year with the County Clerk, County Superintendent of Schools, Board of Governors, and State Department of Finance. The filing date may be extended until December 31 upon written approval of the County Superintendent of Schools. Because district audits include evaluations of major federal programs, copies of the reports must also be submitted to the Federal Bureau of the Census.

Districts do not always submit their audit reports by the established deadline or include all of the required statements and attestations. For the 1987-88 fiscal year, all community colleges districts conducted the required audits, and 69 districts filed the reports in a timely manner. Of those, 50 were submitted by December 31, 1988, while 16 were submitted in January and 3 in February of 1989. Twelve districts did not include all the required information in their initial audit reports, but subsequently corrected the omissions upon notification by the Chancellor's Office. (Appendix B describes the general procedures followed and provides samples of the documents used by the Chancellor's Office to review contracted district audit reports and resolve audit citings.)

As shown in Table 1, district audits for 1987-88 contained 495 citings. Of those, 88 concerned State-compliance areas, 144 applied to State General Apportionment and categorical programs, and 263 dealt with internal controls.

Table 1

Annual Audits
Summary of Audit Citings
Fiscal Year 1987-88

District	Total Audit Citings	Category of Citings		
		State Compliance	Apportionment/ Categorical	Internal Controls
ALLAN HANCOCK JOINT	3	0	1	2
ANTELOPE VALLEY	1	0	1	0
BARSTOW	5	2	1	2
BUTTE	8	3	3	2
CABRILLO	0	0	0	0
CERRITOS	3	1	0	2
CHAFFEY	7	3	0	4
CITRUS	6	2	1	3
COACHELLA VALLEY	0	0	0	0
COAST	9	2	0	7
COMPTON	29	7	9	13
CONTRA COSTA	4	1	0	3
EL CAMINO	16	2	5	9
FEATHER RIVER	0	0	0	0
FOOTHILL-DE ANZA	0	0	0	0
FREMONT-NEWARK	2	0	0	2
GAVILAN JOINT	10	1	6	3
GLENDALE	9	1	0	8
GROSSMONT CUYAMACA	8	0	0	8
HARTNELL	2	1	0	1
IMPERIAL	1	1	0	0
KERN	4	0	1	3
LAKE TAHOE	9	3	1	5
LASSEN	6	3	2	1
LONG BEACH	4	1	0	3
LOS ANGELES	17	4	4	9
LOS RIOS	1	1	0	0
MARIN	9	0	1	8
MENDOCINO LAKE	3	1	1	1
MERCED	12	4	4	4
MIRA COSTA	0	0	0	0
MONTEREY PENINSULA	7	2	4	1
MT. SAN ANTONIO	4	3	1	0
MT. SAN JACINTO	5	1	1	3
NAPA VALLEY	5	1	3	1

Table 1
(continued)

Annual Audits
Summary of Audit Citings
Fiscal Year 1987-88

District	Total Audit Citings	Category of Citings		
		State Compliance	Apportionment/ Categorical	Internal Controls
NORTH ORANGE COUNTY	7	1	2	4
PALO VERDE	19	3	8	8
PALOMAR	5	0	1	4
PASADENA AREA	10	3	2	5
PERALTA	20	2	5	13
RANCHO SANTIAGO	5	0	1	4
REDWOODS	14	3	5	6
RIO HONDO	0	0	0	0
RIVERSIDE	2	1	1	0
SADDLEBACK	5	0	2	3
SAN BERNARDINO	30	0	16	14
SAN DIEGO	6	0	2	4
SAN FRANCISCO	15	1	7	7
SAN JOAQUIN DELTA	0	0	0	0
SAN JOSE-EVERGREEN	1	1	0	0
SAN LUIS OBISPO COUNTY	7	3	1	3
SAN MATEO COUNTY	3	0	1	2
SANTA BARBARA	2	0	0	2
SANTA CLARITA	0	0	0	0
SANTA MONICA	9	0	5	4
SEQUOIAS	9	5	1	3
SHASTA-TEH.-TRI. JOINT	28	5	8	15
SIERRA JOINT	8	1	1	6
SISKIYOUS	6	1	2	3
SOLANO COUNTY	4	0	0	4
SONOMA COUNTY	4	0	1	3
SOUTH COUNTY	6	1	2	3
SOUTHWESTERN	7	1	0	6
STATE CENTER	9	1	2	6
VENTURA COUNTY	14	0	8	6
VICTOR VALLEY	5	0	2	3
WEST HILLS	3	1	0	2
WEST KERN	2	0	1	1
WEST VALLEY-MISSION	13	0	6	7
YOSEMITE	2	2	0	0
YUBA	6	1	1	4
STATEWIDE	**495**	**88**	**144**	**263**

Citings in these three categories are matters of State jurisdiction that fall within the purview of the Chancellor's Office. The office monitors the resolution of these citings to determine what action districts have taken to implement the auditors' recommendations. The office then evaluates each district's response and either verifies that appropriate action is being taken to achieve compliance or initiates further contact with the district to resolve the issue.

Citings concerning internal accounting controls are generally considered to be matters for local resolution. Past experience indicates that districts are usually eager to implement recommendations for strengthening internal controls. The Chancellor's Office may become involved in these resolutions if citings indicate systemwide problems that need to be addressed through amendments to the *Budget and Accounting Manual* or other State publications.

Citings that indicate a district is in or headed toward financial difficulty are referred to as "going concern issues." These issues may be identified in the audit report by a comment or citings regarding the district's ability to meet its financial obligations. Although such issues are matters for State concern, auditors usually report them as internal control problems relating to general accounting or budgeting procedures.

As discussed in Section II, the Chancellor's Office is responsible for identifying and monitoring the financial condition of community college districts. The review and analysis of district audit reports described here represents just one of the elements in the early-warning mechanism that has been developed for that purpose.

The 88 citings in the area of State compliance were found in 43 (62 percent) of the 69 reporting districts. As shown in Table 2, the most frequent citings were in three categories: State Aid for Course Repetition (25); Census and Drop Procedures (14); and Student Probation and Dismissal (10).

State Aid for Course Repetition concerns districts' methods for identifying students who repeat courses. With the majority of district funding derived from State General Apportionment, the Chancellor's Office is concerned that districts procedures for monitoring course repetitions are in general agreement with State regulations. Census and Drop Procedures concern methods used to determine the status of students for purposes of attendance reporting. Student Probation and Dismissal monitors district compliance with regulations dealing with student scholastic standings, a matter that has received increased emphasis with the advent of matriculation programs and community college reform legislation (AB 1725). (See "Looking to the Future".)

Table 3 identifies by category the 144 citings in State General Apportionment and Categorical Programs. These citings were found in the audits of 46 (66 percent) of the reporting districts. Student Loan and Grant Programs accounted for 73 (50 percent) of these citings, which generally occurred because districts lacked adequate loan collection procedures. Auditors also reported 29 instances of

Table 2

Annual Audits
State Compliance Citings
Fiscal Year 1987-88

Categories	Districts Cited	Audit Citings
Audit Trail Accountability	9	9
State Aid for Course Repetition	20	25
Residency Determination	6	6
Census and Drop Procedures	13	14
Salaries of Classroom Instructors	3	3
Excess Costs of Special Courses for the Disabled	2	5
Student Probation and Dismissal	10	10
Allocation of Costs	6	6
Administrative Salaries of EOPS Funded Personnel	0	0
Instructional Equipment	5	5
Other Categories	4	5
STATEWIDE	**43***	**88**

* A district may have received more than one audit citing.

Table 3

Annual Audits
Apportionment and Categorical Citings
Fiscal Year 1987-88

Categories	Districts Cited	Audit Citings
General State Apportionment	19	21
Vocational Education	15	29
Extended Opportunity Programs and Services	3	5
Student Loan Program	30	73
Other Categorical Programs	9	16
STATEWIDE	**46***	**144**

* A district may have received more than one audit citing.

noncompliance in Vocational Education Programs, and 21 instances of noncompliance or computational error in State General Apportionment.

Increasing the effectiveness of contracted district audits is a continuing priority for the Chancellor's Office. Staff has worked closely with the Department of Finance to keep the audit guide current and has become more closely involved with professional organizations interested in community college administration.

In 1988, the Chancellor's Office and the Department of Finance jointly issued a new *Standards and Procedures for Audits of California Community Colleges*, informing

districts and auditors of changes in financial reporting requirements and compliance areas for the 1987-88 and 1988-89 fiscal years. Two State compliance areas were dropped and two new ones were added. The new areas, Student Probation and Dismissal and State Aid for Course Repetition, replaced Course Approval and Courses Eligible to be Offered as Independent Study, which were deleted to keep unchanged the estimated time needed to review State-compliance areas. Revisions were made to clarify three other compliance areas – State Instructional Equipment, federal Vocational Education Programs, and State Joint Training Partnership Programs – and to add suggested compliance audit procedures for Child Development Programs.

In addition, auditors were asked to describe their citings in greater detail and to obtain district responses to the citings, so as to allow for more definitive follow-up by the Chancellor's Office. Further, under provisions of the new guide, district superintendents are to submit written assessments of audit reports similar to those prepared by presidents of large publicly owned corporations. Also, because of revisions in regulations for audits of educational and training programs that receive significant federal funding, district auditors are required to provide positive assurance statements regarding districts' internal control procedures. Previously, such assurances were assumed to be implicit in the general statements concerning internal controls.

Because of significant changes made to the *Standards and Procedures* manual, special efforts were made to familiarize accounting staff, auditors, and admissions and records staff in community college districts with the new audit requirements. Accordingly, the Chancellor's Office and the Department of Finance presented a series of audit forums at six locations throughout the State during the summer of 1988. Almost 300 participants attended the six forums. Topics included an overview of major changes to the *Standards and Procedures* manual, reporting requirements under federal Circular A-128 of the Office of Management and Budget (OMB), introduction to the Fiscal Stability Program, and issues commonly found in attendance audits. The forums signify a major commitment by the Chancellor's Office and the Department of Finance to improved audit quality.

The forums were not the only activities initiated last year to further community college accountability. The California Association of Community College Registrars and Admissions Officers (CACCRAO) sponsored a presentation at its regularly scheduled Southern California meeting at which Chancellor's Office staff addressed three topics: AB 1725 and its effects on admissions and records, auditing requirements for computerized registration systems and file retention requirements. At another meeting, the Southern California section of the California Association of Schools Business Officials (CASBO) sponsored a presentation by Chancellor's Office staff on how revisions are made to the contracted district audit guide, dealing with the new State-compliance issues, and financial reporting under OMB Circular A-128.

II ▸ Fiscal Stability Monitoring System

Over the past decade, California's community colleges have been confronted by a series of fiscal crises. The impact of such factors as high inflation and interest rates, Proposition 13, a cap on funding community college enrollment growth, student enrollment fees, defunding of courses, declining enrollments, increases in State-mandated programs, and the Gann Limit (Proposition 4) have challenged the colleges' ability to maintain existing programs and services. These economic pressures also have brought some districts to the brink of fiscal insolvency and required others to seek emergency state appropriations.

In response to these fiscal difficulties, and with the encouragement of the Board of Governors and other groups, legislation was enacted to foster sound financial management of community college districts. Assembly Bill 2910 (Chapter 1486, Statutes of 1986) requires districts to submit quarterly reports on their financial condition to the Chancellor's Office. AB 2910 assigns to the Chancellor's Office the responsibility of identifying districts at risk and, when necessary, the authority to intervene to bring about fiscal stability. In September 1987, the Board of Governors adopted a policy statement, "Expectations for Sound District Financial Management," setting forth a series of fundamental financial planning and management principles.

To carry out the provisions of AB 2910 and promote the principles set forth by the Board, the Chancellor directed staff to design and implement a comprehensive system for monitoring and evaluating the financial condition of community college districts. Its purpose is to promote fiscal stability through early identification of districts at risk and application of appropriate corrective action that enables those districts to maintain or restore stability. In cooperation with the districts, the Chancellor's Office has designed and is refining a number of instruments and processes to develop comprehensive district fiscal profiles and identify districts that may need assistance.

These general objectives have been reinforced by the passage of AB 1725 (Chapter 973, Statutes of 1988), which will bring about major reforms in the community college system. One of the key provisions the legislation is the assessment of community colleges' effectiveness, as measured on the basis of selected fiscal and educational factors. Implementation of the systemwide Management Information System will assist in achieving this goal.

The present fiscal stability system assesses each community college district's financial condition on the basis of historical and current information derived from multiple sources, such as the district's *Annual Financial and Budget Report* (CCSF-311), annual audit reports, quarterly financial reports, and site visits. An element to be developed is long-term projection of fiscal trends for each district. The

system for monitoring and evaluating fiscal stability provides a needed service to districts by helping them maintain sound fiscal conditions.

Chancellor's Office staff has evaluated the last five quarters of districts' operations and are pursuing follow-up action on 14 districts. Of the 14, only one has been placed in the "high-risk" category, while the other six have been classified as moderate risks. The one high-risk district has recently shown signs of improvement and the Chancellor's Office is working to ensure continued corrective action. Administrative efforts in the 13 other districts identified as "not stable" are preventive in nature.

III ▶ Attendance Audits

Audits of district attendance accounting and reporting procedures determine whether Apportionment Attendance Reports (CCFS-320) and the Annual Apprenticeship Attendance Reports (CCFS-321) have been completed in conformance with applicable laws, regulations, and procedures. The importance of these reviews lies in the fact that the two reports serve as the basis for allocating State General Apportionment in excess of $1 billion a year to community college districts. Attendance audit reports identify inappropriate procedures and errors in the calculation of average daily attendance (ADA) and apprenticeship hours.

The Department of Finance (DOF) is responsible for conducting attendance audits under the general authority provided in the *Government Code* (Sections 13070, 13293, and 13294) and the *Education Code* (Section 84040.5). The department audits between seven and twelve districts a year, which means that each is audited approximately once every five years. The audits focus strictly upon student attendance accounting and related State regulations, in contrast to the other types of audits and reviews discussed in this report.

Based on the information provided by DOF and the audited districts, the Chancellor's Office – under authority of Title 5, Section 58300 of the *Administrative Code* – evaluates each citing and determines how statutes and regulations should apply in specific situations. The office then determines the appropriateness of each DOF recommendation and the amount of adjustment to a district's reported attendance. Once the citings are resolved, the district is notified of the Chancellor's decision on attendance and funding adjustments, if required.

DOF completed seven attendance audits during 1987. Results of five audits were reported in last year's report on fiscal accountability. Four other districts were audited in 1988. Because of the complexity of issues cited by DOF, staff efforts in 1988 dealt with resolving citings for two fiscal years. Hence, Table 4 on the following page presents information from the eleven reports.

There were 88 audit citings and totals of 3,353 credit and 137 noncredit units of claimed ADA cited by DOF. Also, 387 apprenticeship hours were questioned. The eleven DOF audits questioned more than $6 million in the State funds to community colleges.

Table 4

Attendance Audits
Citing Summary
Fiscal Years 1985-86 and 1986-87

Categories	Districts Cited	Audit Citings	Questioned Revenue
Academic Standards	1	1	$3,806
Attendance Clerical Errors	9	19	(133,388)
Attendance Documentation	8	12	109,668
Course Eligibility/Approval	6	7	1,284,368
Courses Limited to Specific Clientele	5	5	131,469
Instructor Certification	9	10	3,759,711
Regulatory Limits/Reporting Controls	11	34	582,246
STATEWIDE	11*	**88**	**$6,007,880**

* A district may have received more than one audit citing.

The most significant citings in terms of potential revenue adjustments involved Instructor Certifications, Course Approvals, Regulatory Limits/Reporting Controls, and Attendance Documentation. DOF cited nine of the eleven districts for instructors teaching courses in subject areas not listed on their credentials. The resolutions of these citings were complex because degrees held by individuals may qualify them to teach a number of different subjects, but the specific subject areas of qualification may not be listed as part of their credentials. Program staff exercised particular discretion in dealing with these issues, aware that the resolutions might possibly influence the principles that will guide implementation of the minimum qualifications that will replace credentials under the provisions of AB 1725.

Six districts were cited for conducting courses not approved or not part of an approved program area. Primarily, these citings identify situations in which districts may have significantly revised their curricula without having such changes approved by proper authorities.

Examples of citings concerning regulatory limits and reporting controls include:

- Inaccurate census and drop procedures that resulted from districts including attendance of inactive students;
- District policies and procedures that were not totally effective in preventing unallowable course repetitions;

- Attendance reporting procedures that were not adequate to insure the maintenance of accurate positive attendance records; and

- Duplicate reporting of course sections.

Citings under Attendance Documentation resulted from districts not adequately documenting course content, student prerequisites, or other student/instructor agreements required in independent study and work experience courses.

Resolution of these citings has involved significant staff examination and research of the facts behind the citings and of existing local practices as compared to legislative intent for community college reform. Such resolutions are complex and require extensive communication with both State and local personnel.

IV ▸ Vocational Education Fiscal and Compliance Audits

The Carl D. Perkins Vocational Education Act (VEA) of 1984, Public Law 98-524, provides federal funds to states to improve and expand vocational education programs and services. To qualify for these funds, states must submit vocational education plans to the U.S. Department of Education describing statewide objectives and uses for the funds. The Act requires each state to designate a single agency to administer the plan, including the disbursement of federal funds.

In California, that designated agency is the State Department of Education. The department allocates and distributes VEA funds in different categories designed to support special types of activities and services at the local level. Based upon a federal regulatory formula, community colleges receive a substantial share of the total funds distributed in California. For the 1987-88 fiscal year, community colleges received a total of $35.5 million in VEA funds. Of that amount, $1.1 million went for statewide administration (Title II of the Act); $21.3 million for support services to special populations (Title II-A); $12.2 million for program improvement (Title II-B); $627,000 for community-based operations (Title III-A); and $316,000 for consumer and homemaker education (Title III-B). Over 87 percent of the funds went directly to the districts. Of the remainder, 9 percent was used for special projects and 3.7 percent for State operations.

Districts that wish to qualify for VEA funding must meet certain compliance and procedural requirements. Three documents must be submitted to the Chancellor's Office by participating districts: (1) a Local Plan for Vocational Education, (2) an Annual Application for VEA Funds, and (3) an Annual Claim for VEA Funds.

The Local Plan is a projection by the district of the most effective use of federal funds to meet the objectives of the Act. It includes an assessment of local needs and serves as a guide for designing programs, services, and activities to meet those needs.

The Annual Application describes the programs, services and activities that are to be paid for with VEA funds. It must address each Title and part of the Act, providing specific information on how the VEA funds will be used.

The Annual Claim is submitted at the end of each fiscal year for reimbursement of the actual costs incurred by the district. These costs are compared to those shown in the Local Plan and the Annual Application.

The focus of accountability in vocational education programs is the Annual Claim. The Chancellor's Office uses several methods to encourage districts to correctly report expenditures and operate proper accountability systems in vocational education programs. Besides the annual audits discussed in Section I, Chancellor's

Office staff conducts fiscal and compliance audits of vocational education programs and examines the appropriateness and accuracy of the district's Annual Claim for reimbursement. These audits also determine whether colleges have sufficient documentation to substantiate their claims and whether they have complied with the applicable federal regulations. Student files are examined to verify that local procedures identify eligible recipients. Community colleges are required to verify the eligibility of students because VEA funds, particularly those under Title II-A and Title III-B, are dedicated to special categories of students, such as those academically disadvantaged or located in economically depressed areas.

VEA fiscal and compliance audits also focus on the nature of services provided with Title II-A and Title III-B funds. Generally, these funds are provided to local educational agencies so that supplemental services can be provided to students with special needs, enabling them to overcome factors that prevent their completing vocational programs. Local educational agencies including community colleges using such funds, are required to document that students are vocational, have special needs and received services that correlated to those special needs. Audit exceptions are typically identified in four general categories: (1) ineligible students, (2) student file documentation, (3) financial records, and (4) ineligible costs.

An audit exception in the "ineligible students" category occurs when a college maintains adequate documentation, but the records indicate that a student was not eligible to receive supplemental vocational services. For example, a student with a nonvocational goal such as transferring to a four-year institution generally would not be considered a vocational student and, therefore, is ineligible for VEA-funded support services.

The second type of audit exception, "student file documentation," indicates that a college has not maintained adequate documentation to substantiate a student's involvement in a vocational program and/or special characteristics that make him or her eligible to receive supplemental services.

When colleges do not maintain adequate documentation to substantiate the services provided, audit exceptions fall into the category of "financial records." An example would be when amounts on the Annual Claim do not correspond to summaries of detailed expenditure records.

The final class of audit exceptions, "ineligible costs," occurs when colleges maintain adequate documentation, but the records indicate that services provided were not appropriate within federal reimbursement guidelines. For example, vocational counseling services provided by an individual who lacks the required counseling education and vocational experience would not be eligible for reimbursement. Another example in this category would be if a college provided tutoring to students whose special needs required transportation or interpreter services instead.

Chancellor's Office staff performed VEA fiscal and compliance audits in nine community colleges and at one private contractor during 1988. As shown in Table 5, these audits found exceptions totaling more than $273,000. The most significant audit exceptions concerned "student file documentation," accounting for almost $158,000 (57 percent) of the total amount cited.

Table 5

Vocational Education
Compliance and Financial Audits
Audit Exceptions Identified During 1988

Program Purposes	Colleges Cited	Total Claims Reviewed	Total Audit Exceptions	Student File Documentation	Ineligible Students	Financial Records	Ineligible Costs
Title II-Statewide Administration	0						
Title IIA-Support Services							
Adults Needing Training	3	$98,162	$20,159	$11,286		$8,873	
Cooperative Work Experience	0						
Disadvantaged	6	427,807	81,390	55,610		19,783	$5,997
Elimination of Sex Bias	5	62,545	29,795	15,337		14,458	
Handicapped	8	217,910	60,260	17,885		36,354	6,021
Limited English Proficiency	5	25,738	24,668	23,553			1,115
Personnel Training/Administration	0						
Single Parents/Homemakers	7	120,684	53,146	32,527		18,658	1,961
Support Services for Women	0						
Vocational Guidance & Counseling	1	6,880	1,147	1,147			
Title IIA-Community-Based Organizations	0						
Title IIB-Program Improvement							
Administration	1	50,510	315	--		315	
Title IIIB-Consumer & Homemaking Ed							
Consumer & Homemaking Education	0	6,105					
Economically Depressed Areas	1	2,875	2,875				2,875
STATEWIDE	**10***	**$1,019,216**	**$273,755**	**$157,345**	**$0**	**$98,441**	**$17,969**

* Colleges may have received more than one audit citing.

While VEA fiscal and compliance audits have had a positive influence upon the administration of local educational programs, efforts need to be expanded. Existing accountability efforts do not provide total reassurance that college programs fully comply with federal requirements, as evidenced in Table 5. VEA audits during 1988 identified no circumstances where ineligible students received federally funded support services. This absence of audit exceptions may appear encouraging, but must be tempered by the results of student file documentation and financial records exceptions, where $255,786 (25 percent) of the total claims reviewed resulted in audit exceptions. Furthermore, student file documentation exceptions represent situations where local administrators did not adequately document fundamental eligibility criteria, vocational program involvement, and the special conditions of students that make them eligible for supplemental support services. Without such documentation, auditors and program administrators cannot be assured that eligible students received services.

To counter these shortcomings and further encourage vocational education accountability, the Chancellor's Office staff publishes the *Documentation Guide for Use of Federal VEA Funds*, which details local documentation requirements, and conducts accountability and application/claim workshops to explain what information must be maintained locally or submitted with the applications and claim. Workshops also have been held to alert contracted district auditors and district staff to changes in the *Standards and Procedures for Audits of California Community Colleges* relative to vocational education programs.

The *Documentation Guide*, first published by Chancellor's Office in 1987, is a quick reference manual for compliance and procedural requirements associated with the federal Act and related State requirements. The *Guide* lists allowable activities under each major program to help colleges identify costs that may be claimed against federal funds. Other sections of the *Guide* explain documentation requirements for each major program component to help colleges maintain evidence that eligible students received appropriate services.

Related staff accountability efforts include application and claim workshops at which changes to procedures or to the *Guide* are communicated to appropriate local staff. In other efforts, Chancellor's Office staff have participated in annual conferences for California Community College Administrators of Occupational Education, and discussions of accountability with staff from individual districts. These efforts attempt to provide those directly responsible for accountability at the local level with an opportunity to examine their operations and procedures and compare their systems with the federal and State compliance requirements in a non-punitive setting.

Looking to the Future

The present financial accountability activities focus upon districts' general financial operations, fiscal stability, and student attendance accounting, as well as the administration of selected categorical programs. Annual district audits provide needed assurances regarding financial activities, but only limited assurances in compliance areas. However, efforts are underway that may have a significant impact upon how audits in general are conducted and reported.

Annual audits in community colleges presently are conducted and reported in accordance with Circular A-128 of the Federal Office of Management and Budget (OMB), "Audits of State and Local Governmental Units." Another set of federal regulations, OMB Circular A-110, stipulate federal reporting requirements for institutions of higher education and other nonprofit organizations. Although, community colleges are institutions of higher education, the State Department of Finance previously has required districts to comply with OMB A-128 rather than OMB A-110, because the second circular does not address audit requirements. That situation appears to be changing.

In December 1988, OMB proposed new federal regulations in its Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Organizations." Once approved, the regulations would apply to institutional audits for Fiscal Year 1989-1990 and thereafter. While the full effect of the new regulations on the present audit guide has not been fully assessed, auditors and district administrators are advised to become familiar with the proposed federal regulations. To assist them in that endeavor, the Chancellor's Office has included the text of these regulations as Appendix C.

On a more local level, the passage of community college reform legislation, Assembly Bill 1725, provides for phasing out the current funding formula and its single workload measure, average daily attendance (ADA). The legislation adds *Education Code*, Section 84750, which requires the establishment of a program-based funding formula. Rather than ADA, the new formula will use full-time equivalent (FTE) students, headcount enrollment, and square footage as workload measures. The implementation of the new funding formula is contingent upon the Legislature appropriating $140 million in new funds to introduce major reforms in the community college system. Such reforms include the development of articulation programs, the replacement of the centrally controlled system of credentials with a locally administered system of minimum qualifications for faculty, and the improvement of instructional quality by reducing class size and increasing the use of full-time instructors.

In another endeavor, the Chancellor's Office has developed a formal Consultation Process that involves, among others, district chief business officers and provides them with the opportunity to comment on proposals that affect the colleges. The membership of the Council of Chief Business Officers (CBO Council) includes the Vice Chancellor for Fiscal Policy from the Chancellor's Office and ten chief business officers, each representing a different region of the State. The current and past presidents of the Board of Directors of the Association of Chief Business Officers, California Community College Districts, also are members of the council.

The role of the CBO Council is to review and comment upon proposed statewide policies and procedures affecting fiscal resources. To that end, a sample Request for Proposal (RFP) for annual audit contracts recently has been developed through consultation. In addition, the council presently is reviewing several topics, including the fiscal stability monitoring system, provisions of the Budget and Accounting Manual, and policies for establishing capital outlay priorities and needs. Proposals developed through the council may result in additional changes to the audit process.

The Chancellor's Office also is continuing to develop a systemwide Management Information System (MIS) in response to the increased emphasis on accountability and the need for accurate information on students, courses, staff, and finances. For this system to be effective, the information collected needs to be accurate and comparable among districts. The project will be phased in over the next several years and is presently concentrating on the collection of student and course information – critical components of a successful matriculation program.

Also, the Chancellor's Office plans to continue field reviews of audit workpapers to provide feedback to annual auditors and to identify potential changes to the audit guide. Annual auditors, district staff, and Chancellor's Office staff benefit from discussions that occur during such field reviews. For example, recent conversations with annual auditors and reviews of CDA reports have revealed that in the last two years auditors have become much more familiar with the technical requirements of community college audits, particularly in the area of categorical programs. This increased sophistication can be attributed, in part, to the increased communication and closer working relationships.

The Chancellor's Office fiscal stability monitoring and evaluation system will focus on the continued refinement of the early warning mechanism and the adoption of statewide fiscal standards through the Consultation Process. The emphasis will be on preventive strategies and standards to assist district trustees and staff in understanding the assessments of their financial strengths and weaknesses. Emphasis also will be placed on coordinating the elements of the monitoring and evaluation system with the requirements of AB 1725 and the systemwide MIS.

The Chancellor's Office is considering a major change in procedures for conducting audits of vocational education and other categorical programs. Currently, compliance audits of these programs are performed independently of one another.

As new categorical programs, such as Greater Avenues for Independence (GAIN) and Basic Skills, are established financial and compliance accountability mechanisms must be developed. Furthermore, vocational education fiscal and compliance audit reports take almost a year to complete and are resolved differently from CDA reports, attendance audits, and compliance reports of other categorical programs. The Chancellor's Office recognizes that audit techniques need to be made more consistent and that audit reports need to be issued in a more timely manner; consequently, staff is reviewing organizational structures, auditing techniques, and reporting procedures and documents used to transmit audit findings.

Appendix A

State Compliance Requirements

COMMUNITY COLLEGES
STATE COMPLIANCE REQUIREMENTS

1987-88 FISCAL YEAR AUDITS

State General Apportionment Testing Structure

1. **Audit Trail Accountability**

Compliance Requirement:

Each district shall maintain a separate and complete tabulation for each course section in which the student attendance is reported for state support.

2. **State Aid for Course Repetition**

Compliance Requirement:

Section 58161 of the *California Administrative Code* does not allow a district to claim State General Apportionment for attendance of a student in a course in which the student has previously received a grade from the district unless either the student is repeating the course to alleviate substandard work which has been recorded on the student's record, the district finds that the student's previous grade was the result of extenuating circumstances, or the district has determined that a student should repeat a course because these has been a significant lapse of time since the student previously took the course.

Attendance for such repetition may be claimed only once for State aid (beyond that originally claimed when the course was first completed). State General Apportionment for repetition of "activity" courses not expressly authorized above may be claimed for three additional semesters or five additional quarters upon approval of the Chancellor.

The district must identify the courses which are to be repeatable and designate such courses in its catalog, and must determine and certify that each identified course is one in which the course content differs each time it is offered, and that the student who repeats it is gaining an expanded educational experience. The district must also develop and implement a mechanism for the proper monitoring of such repetitions. (For the 1987-88 fiscal year, the Chancellor has delegated authority to the districts to designate activity courses as repeatable consistent with

applicable standards developed in Section 58161 of Title 5 of the *California Administrative Code*.

3. Residency Determination

Compliance Requirement:

Each district must act to ensure that the residency of each student is properly classified and that only the attendance of California residents is claimed for state support.

4. Census and Drop Procedures

Compliance Requirement:

Each district shall claim for apportionment purposes only the attendance of students actively enrolled in a course section as of the census date (if census procedures are used to record attendance in the course section).

Annual Compliance Focus

5. Salaries of Classroom Instructors

Compliance Requirement:

Each district's salaries of classroom instructors shall equal or exceed 50 percent of the district's Current Expense of Education in accordance with Section 84362 of the *Education Code*.

6. Excess Costs of Special Courses for the Disabled

Compliance Requirement:

Each district's claim for state excess cost funds to partially support special classes for the disabled shall not exceed an amount equal to the total direct cost of eligible courses less all regular state apportionments received for student attendance in these courses.

7. Student Probation and Dismissal

Compliance Requirement:

Students shall be placed on probation if their grades reflect either academic deficiency or failure to make timely progress on courses attempted or earned a grade point average below 2.0 in at least 12

semesters or 18 quarter units attempted or entries of "W," "I," and "NC" in at least 50 percent of 12 semesters or 18 quarter units attempted. Students on probation shall be subject to dismissal if they each earned either an accumulative grade point average of less than 1.75 in all units attempted over three semesters or five quarters; or receive entries of "W," "I," or "NC" in at least 50 percent of units attempted over three semesters or five quarters.

8. **Allocation of Costs**

Compliance Requirement:

Salaries of instructors teaching ADA-generating classes, school counselors providing academic advisement, and financial aid officers conducting need analysis are not considered supportable charges against either Extended Opportunity Programs and Services (EOPS) or Handicapped Student Programs and Services (HSPS) accounts unless their activities require them to perform additional functions for the EOPS or HSPS programs which are beyond the scope of services provided to all students in the normal performance of the regular duty assignments. These activities may be supported only to the extent of the supplementary services provided for EOPS or HSPS.

9. **Administrative Salaries of EOPS Funded Personnel**

Compliance Requirement:

Each district's claim upon EOPS funds shall exclude expenses incurred as administrative salaries (assistant dean beginning salary level for the district and above) unless the administrator exclusively functions in the capacity of the EOPS Director or an exemption is specifically certified by the State Chancellor's Office.

10. **Instructional Equipment**

Compliance Requirement:

Each district shall use instructional equipment funds to purchase equipment for instructional purposes to satisfy any of the following objectives:

- Replace old equipment with property of a similar nature,
- Upgrade existing equipment to bring an instructional program to state-of-the-art quality,

- Expand existing equipment to serve additional students,
- Change dimensions of a program by changing the emphasis or objective of an instructional program in some way.

Appendix B

Annual Audit Report Review and Citing Resolution Procedures

Illustrations

Illustration 1 -- (FSWS-270) Check List for Completeness of Audit Report

Illustration 2 -- Letter to District Business Manager Requesting Information Omitted from the Audit Report

Illustration 3 -- (FSWS-260) Audit Report Citings List

Illustration 4 -- Letter to District Business Manager Requesting District Response to State Jurisdictional Audit Citings

Illustration 5 -- Instructions for Completion, Form FSWS-280

Illustration 6 -- (FSWS-280) Restatement of Each State Jurisdictional Audit Citing Requesting District Response

ANNUAL AUDIT REPORT REVIEW AND CITING RESOLUTION PROCEDURES

1. Objectives of the Audit Report Review

The Chancellor's Office has developed a three-part review and follow-through process for annual audit reports to determine:

What prescribed information, if any, has been omitted from the contracted district audit (CDA) report and thus still needs to be supplied by the district.

What local management issues have been identified by the independent auditor and whether the district has taken appropriate action to implement recommendations to resolve the issues.

What state jurisdictional issues have been identified by the independent auditor, what the district has done about these findings since the audit, and what if anything further needs to be done to ensure district compliance and the equity of state and federal apportionments and allowances.

2. Identification and Elimination of CDA Report Omissions

When the CDA report is first received, the Chancellor's Office reviews, evaluates and identifies the completeness of each report by determining whether each statement and schedule prescribed in the *Standards and Procedures for Audits of California Community Colleges* is included in the auditor's report (ILLUSTRATION 1). Also, the initial review alerts Chancellor's Office staff to districts where independent auditors may be concerned about the district's ability to meet its financial obligations.

If the CDA report does not contain all the statements and auditor's reports required by the audit guide, the Chancellor's Office informs the district about the nature of the omissions (ILLUSTRATION 2).

In cases where the independent auditor makes statements about a districts continued existence or its ability to meet its financial obligations, audit reports are immediately transmitted to other Chancellor's Office staff in the Fiscal Stability and Monitoring Program for further evaluation and communication directly with the districts as needed.

Districts are requested to correspond within two weeks either confirming that an omission exists and providing the information/explanation necessary to complete the review or showing the inapplicability of the required statement.

3. Identification and Reporting of CDA Citings

The second review phase requires Chancellor's Office staff to summarize the citings and recommendations on Form FSWS-260 (ILLUSTRATION 3) and transmit individual citing information to the districts for review and response on Form FSWS-280 (ILLUSTRATIONS 4, 5 and 6).

Each district is requested to return the completed FSWS-280s within one month of receipt. On those forms, districts determine whether each citing is implemented, in the process of being implemented or has not been implemented.

4. Clarification and Resolution of CDA Citings Within the State's Jurisdiction

In the final review phase, Chancellor's Office staff review district responses on the FSWS-280s to CDA state jurisdictional issues to determine whether districts have satisfactorily addressed each citing. If staff agree that a citing has been satisfactorily addressed, it is considered resolved. If the adequacy of the district's response is questioned, the citing is referred to an audit review committee within the agency to determine collectively what further district action is necessary.

After consensus is reached, a letter is transmitted to the district detailing what corrective action must be taken to resolve the citing. The transmittal may require the district to elaborate or update its response. The letter also may include appropriate timeframes within which the action must occur.

Upon receipt of the second district response, as necessary, the audit review committee determines whether action taken by the district is sufficient to resolve the citing. If the committee determines that it is, the district is so notified and the issue is considered resolved. If it is determined that the issue remains unresolved, a second letter seeking corrective action is transmitted to the district. This cycle of district responses and evaluation of responses continues until satisfactory resolution is achieved.

CHANCELLOR'S OFFICE
COMMUNITY COLLEGES – FISCAL SERVICES
CONTRACTED DISTRICT AUDIT REPORT
REPORT PERIOD 1987-88

CHECK LIST FOR COMPLETENESS OF AUDIT REPORT

DISTRICT NAME: _____ **FISCAL YEAR:** 1987-88

ACCOUNTING FIRM: _____

I. **DISTRIBUTION OF AUDIT REPORTS**

A Report Receipt Date: _____
B On Time _____ Late: (1) _____ (2) _____ (3+) _____

II. **REPORTING REQUIREMENTS**

A _____ District Superintendent's Message
B _____ Auditor's Report on Internal Control
C _____ Auditor's Report on Internal Controls for Federal Programs
D _____ Auditor's Report on State Compliance
E _____ Auditor's Report on Federal Compliance
F _____ Findings and Recommendation
G _____ Auditor's Report on Financial Statements
H _____ District Financial Statements
I _____ Notes to the Financial Statements
J _____ Auditor's Report on Supplemental Information
K _____ Supplemental Information
L _____ Status of Prior Year Findings And Recommendations

III. **COMPLETENESS OF AUDIT REPORT**

A Complete _____
B Incomplete _____

IV. **FISCAL STABILITY COMMENT** YES _____ NO _____

COMMENTS

_____

_____

_____

_____

Reviewed By _____ Date: _____

ILLUSTRATION 2

CHANCELLOR'S OFFICE
GEORGE DEUKMEJIAN, Governor

CALIFORNIA COMMUNITY COLLEGES
1107 NINTH STREET
SACRAMENTO, CALIFORNIA 95814
(916) 445-8752 445-1163

MEMORANDUM

To: Chief Business Officer

From: Gary L. Cook, Administrator
Fiscal Services

Re: 1987-88 Contracted District Audit

Synopsis: We have reviewed your districts 1987-88 Contracted District Audit (CDA) report for conformance with the reporting requirements of the Standards and Procedures Manual as published by the Department of Finance.

In this preliminary review of your audit report, we note the following omission(s):

- oReport on Internal Controls for Federal Programs.
- o_____
- o_____

Action/Date Requested: This information is necessary for your audit report to be considered complete. Please provide the requested information within two weeks of receipt of this letter.

Your early response to this request is appreciated.

Contact: If you have any questions regarding requirements, please contact Walt Reno of my staff at (916) 445-1163.

GLC:ai

cc: District Superintendent
County Superintendent of Schools
Douglas W. Burris
Walt M. Reno
cletter

CHANCELLOR'S OFFICE
COMMUNITY COLLEGES – FISCAL SERVICES
CONTRACTED DISTRICT AUDIT REPORT

AUDIT REPORT CITINGS LIST

DISTRICT NAME: _____ **FISCAL YEAR:** 1987-88

ACCOUNTING FIRM: _____

ITEM	CODE	TYPE	COMMENTS

ITEM: Sequential Numbering of Citings

CODE: (1) Findings and Auditor Recommendation; (2) District Response; (3) Reviewer's Comment

TYPE: (A) Compliance; (B) Apportionment; (C) Internal

Prepared By: _____ Date: _____ Reviewed by: _____

ILLUSTRATION 4

CHANCELLOR'S OFFICE

GEORGE DEUKMEJIAN, Governor

CALIFORNIA COMMUNITY COLLEGES
1107 NINTH STREET
SACRAMENTO, CALIFORNIA 95814
(916) 445 8752 445-1163

MEMORANDUM

To: Chief Business Officer
title
association
address
city, state zip

From: Joseph M. Freitas, Director
Fiscal and Program Standards Accountability

Re: 1987-88 Contracted District Audit

Synopsis: We are required by Education Code Section 84040 to review each district's annual Contracted District Audit (CDA) report to: (1) determine conformance with reporting requirements, (2) identify audit citings and obtain district responses, and (3) provide agency follow-up on those citings involving district compliance and eligibility for State and federal funds.

Generally, audit citings concerning internal controls are considered local management issues. As such, a district is to implement auditors' recommendations that strengthen internal controls. In instances where internal control citings concern multiple-year citings with fiscal impacts, going concern issues, or potentially illegal acts, we elect to classify the issues as state jurisdictional citings requiring district response. For other internal control citings, we rely on auditors' observations reported in subsequent audit reports.

Action/Date Requested: To meet the first requirement, we have reviewed the audit report and found that it was generally understandable and in conformance with the reporting requirements. In order for us to complete the second and third requirements, you are requested to provide the Chancellor's Office with information on the current status of your 1987-88 CDA Report state jurisdictional citings. To assist you, a Form FSWS-280 is attached for each citing. Each form is to be completed and returned to us within one month from the date of this letter.

Questions should be addressed to Walt M. Reno at (916) 445-1163.

GLC:WR:ai

Attachments

cc: District Superintendent (letter only)
County Superintendent of Schools (letter only)
Douglas W. Burris (letter only)
Walt M. Reno

c2801tr

INSTRUCTIONS FOR COMPLETION
FORM FSWS-280
CONTRACTED DISTRICT AUDIT REPORT
AUDIT CITINGS AND DISTRICT RESPONSE
1987-88 FISCAL YEAR

1. Review the audit citing recommendation and determine status of district actions. (Reference to the audit report may be necessary.)

2. Check the appropriate box indicating the district's current status of implementing the auditor's recommendation and explain action taken. If district responded to citing/recommendation in audit report, please verify the response and check the appropriate box to indicate current status.

3. Sign and date the form.

4. Submit one copy within one month from the date of letter to:

   Chancellor's Office
   Fiscal Services Unit
   1107 Ninth Street, Suite 500
   Sacramento, CA 95814

As in the past, the Chancellor's Office will determine what action is required by way of our follow-through activities on those citings involving district eligibility for State and federal funds. The district will be contacted as necessary to insure appropriate resolution and accountability. It is the district's responsibility to provide information to the county superintendent of schools, as appropriate. Your cooperation is appreciated.

CHANCELLOR'S OFFICE
COMMUNITY COLLEGES – FISCAL SERVICES
CONTRACTED DISTRICT AUDIT REPORT

COMMUNITY COLLEGE DISTRICT
AUDIT CITINGS AND DISTRICT RESPONSE
1987-1988 FISCAL YEAR

AUDIT CITING/RECOMMENDATION

DISTRICT RESPONSE

( ) IMPLEMENTED; ( ) BEING IMPLEMENTED; ( ) NOT IMPLEMENTED

BUSINESS MANAGER'S
SIGNATURE: _____ **DATE:** _____

FSWS 280

Appendix C

Office of Management and Budget, Circular A-133: Audits of Institutions of Higher Education and Other Nonprofit Organizations; Notice

federal register

Thursday
November 10, 1988

Part VII

Office of Management and Budget

Audits of Institutions of Higher Education and Other Nonprofit Organizations; Notice

OFFICE OF MANAGEMENT AND BUDGET

(Proposed Circular No. A-133)

Audits of Institutions of Higher Education and Other Nonprofit Organizations

AGENCY: Financial Management Division, OMB.

ACTION: Proposed Circular No. A-133 "Audits of Institutions of Higher Education and Other Nonprofit Organizations".

SUMMARY: This notice offers interested parties an opportunity to comment on a new circular, "Audits of Institutions of Higher Education and Other Nonprofit Organizations". The revision would supersede Attachment F subparagraph 2h of Circular A-110 "Uniform Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and Other Nonprofit Organizations".

The change in audit policy arises from a commitment made by OMB during Congressional consideration of the Single Audit Act of 1984, Pub. L. 98-502. At that time Congress agreed to exclude most colleges and universities from coverage under the Act. OMB agreed to develop an audit policy for these organizations consistent with the provisions of the Act.

The revised audit policy will require an independent annual audit of the organization in accordance with generally accepted government auditing standards and the provisions of the Circular. The revised audit policy covers:

—Scope of audit,
—Internal control reviews,
—Compliance reviews,
—Relationship to other audit requirements,
—Federal cognizant agency responsibilities,
—Reporting illegal acts of irregularities,
—Audit reports,
—Audit resolution,
—Retention of audit workpapers and reports,
—Audit costs,
—Sanctions, and
—Auditor selection.

The audit provisions of Circular A-110 are being published separately from the uniform agency regulations replacing Circular A-110 for more effective administration of audit policy. If the audit requirements for recipients were published in the uniform rules a separate Circular would still be necessary for Federal audit responsibilities and fragment the overall audit approach. This proposed Circular is patterned after Circular A-128 "Audits of State and Local Governments," which has become familar to the audit and grantee community and is generally being implemented effectively. The proposed Circular helps tailor requirements to the recipient and generally avoids confusion.

All interested parties are encouraged to make their views known.

FOR FURTHER INFORMATION CONTACT: Palmer Marcantonio, Financial Systems and Policy Branch, Office of Management and Budget, Washington, DC 20503, 202-395-3991.

Comments should be received within 60 days of this notice. All comments should be submitted to the above individual.

Sincerely,

Gerald R. Riso,

Associate Director for Management.

[OMB Circular No. A-133, 1988]

To the Heads of Executive Departments and Establishments

Audits of Institutions of Higher Education and Other Nonprofit Institutions

1. *Purpose.* This Circular establishes audit requirements for institutions of higher education and other nonprofit institutions receiving Federal funds. It also defines Federal responsibilities for implementing and monitoring these requirements. The term "nonprofit institutions" used throughout the Circular includes institutions of higher education. The term does not include hospitals, or State and local governments and Indian tribes covered by Circular A-128 "Audits of State and Local Governments."

2. *Authority.* This Circular is issued under the authority of the Budget and Accounting Act of 1921 as amended; the Budget and Accounting Procedures Act of 1950, as amended; Reorganization Plan No. 2 of 1970 and Executive Order No. 11541.

3. *Supersession.* This Circular supersedes Attachment F, subparagraph 2h, of Circular A-110, "Uniform Administrative Requirements for Grants and other Agreements with Institutions of Higher Education, Hospitals, and other Nonprofit Organizations."

4. *Policies.*

a. Nonprofit institutions that receive $100,000 or more a year in Federal funds shall have an audit made in accordance with this Circular.

b. Nonprofit institutions that receive Federal awards between $25,000 and $100,000 a year shall have an audit made in accordance with this Circular or have an audit made of each Federal award.

c. *Subrecipients.* All subrecipients of Federal financial assistance receiving more than $25,0000 in Federal awards are subject to those Federal audit requirements applicable to that particular subrecipient.

d. *Cognizant Agencies.*

(1) OMB will assign a Federal agency to each of the larger nonprofit institutions as the cognizant agency for monitoring audits, and overseeing the resolution of audit findings that affect the programs of more than one agency. Smaller nonprofit institutions not assigned a cognizant agency will be under the general oversight of the Federal agency that provides them with the most funds.

(2) Federal cognizant agency assignments for carrying out the responsibilities in this section are set forth in a separate supplement. Government-owned, contractor-operated facilities at nonprofit institutions are not included in the cognizance assignments. These will remain the responsibility of the contracting agencies. The listed assignments cover all of the functions in this Circular unless otherwise indicated. The Office of Management and Budget will coordinate changes in agency assignments.

5. *Scope of Audit*

a. The audit shall be made by an independent auditor in accordance with Government Auditing Standards covering financial audits. The audit should be an organization-wide audit of the nonprofit institution. However, a coordinated audit approach which tailors the scope of the audit to individual circumstances may be worked out between the recipient and the cognizant agency or the agency providing the most funds to a recipient when a cognizant agency has not been assigned. Any agreements concerning coordinated audits reached between cognizant agencies and recipients should be cleared with other Federal agencies providing funds.

b. States and local governments may include public colleges and universities in audits performed in accordance with OMB Circular A-128 "Audits of State and Local Governments". However, such audits of these entities when made as part of the States A-128 audit should include the additional audit requirements in this Circular.

c. The auditor shall determine whether:

(1) the financial statements of the institution present fairly its financial position and the results of its financial

operations in accordance with generally accepted accounting principles;

(2) the institution has an internal accounting and other control structure to provide reasonable assurance that it is managing Federal awards in compliance with applicable laws and regulations; and

(3) the institution has complied with laws and regulations that may have material effect on its financial statements and on each major Federal award program.

6. *Applicability.* The provisions of this Circular apply to all Federal agencies responsible for administering programs that involve grants, contracts and other agreements with institutions of higher education and other nonprofit recipients. These principles, to the extent permitted by law, constitute guidance to be applied by agencies consistent with and within the discretion, conferred by the statutes governing agency action.

7. *Definitions.* For the purposes of this Circular the following definitions apply:

a. "Award" means financial assistance, and Federal cost type contracts used to buy services or goods for the use of the Federal Government. It includes awards received directly from the Federal agencies or indirectly through other grantees. It does not include procurement contracts under grants or subcontracts used to buy goods or services. Audits of such government contracts shall be covered by the terms and conditions of the contract.

b. "Cognizant agency" means the Federal agency assigned by the Office of Management and Budget to carry out the responsibilities described in paragraph 10 of this Circular.

c. "Federal agency" has the same meaning as the term "agency" in section 551(1) of Title 5, United States Code.

d. "Financial assistance" means assistance provided by a Federal agency in the form of grants, contracts, cooperative agreements, loans, loan guarantees, property, interest subsidies, insurance, or direct appropriations, but does not include direct Federal cash assistance to individuals. It includes awards received directly from Federal agencies, or indirectly through other recipients.

e. "Generally accepted accounting principles" has the meaning specified in the generally accepted government auditing standards.

f. "Government Auditing Standards" means the *Standards For Audit of Government Organizations, Programs, Activities, and Functions*, developed by the Comptroller General, dated July 1988.

g. "Independent auditor" means:

(1) A State or local government auditor who meets the independence standards specified in generally accepted government auditing standards; or

(2) A public accountant who meets such independence standards.

h. "Internal control structure" means the plan of organization and methods and procedures adopted by management to ensure that:

(1) Resources use is consistent with laws, regulations, and policies;

(2) Resources are safeguarded against waste, loss, and misuse; and

(3) Reliable data are obtained maintained, and fairly disclosed in reports.

i. "Major program" means an individual award or a number of awards in a category of Federal assistance or support on which the auditor will be required to express an opinion as to whether the major program is being administered in compliance with laws and regulations.

(1) Universities:

(a) Each of the following categories of Federal awards shall constitute a major program:

—Research and Development,

—Student Aid,

—Individual awards (not in the student aid or research and development category) for which Federal expenditures during the applicable year exceed the larger of 3 percent of the total Federal funds received (other than research and development and student aid) or $100,000.

(2) Other nonprofit organizations:

A major program for nonprofit organizations means any program for which Federal expenditures during the applicable year exceed the larger of $100,000 or 3 percent of such total expenditures.

j. "Subrecipient" means any person or government department, agency, establishment or nonprofit organization that receives Federal financial assistance to carry out the program through a primary recipient, but does not include an individual that is a beneficiary of such a program. A subrecipient may also be a direct recipient of Federal awards.

8. *Frequency of audit.* Audits shall be made annually unless the recipient is audited as part of the State or local government that have previously made other arrangements with the Federal Government.

9. *Internal control and compliance reviews.* The independent auditor shall determine and report on whether the recipient has internal control systems to provide reasonable assurance that it is managing Federal awards in compliance with applicable laws, regulations and contract terms.

a. *Internal control review.* In order to provide this assurance on internal controls the auditor must make a study and evaluation of internal control systems used in administering Federal awards. The study and evaluation must be made whether or not the auditor intends to place reliance on such systems. As part of this review, the auditor shall:

(1) Test whether these internal control systems are functioning in accordance with prescribed procedures.

(2) Examine the recipient's system for monitoring subrecipients and obtaining and acting on subrecipient audit reports.

b. *Compliance review.* The auditor should determine whether the recipient has complied with laws and regulations that may have a material effect on each major Federal program.

(1) In order to determine which major programs are to be tested for compliance, recipients shall identify in their accounts all Federal funds received and expended and the programs under which they were received. This shall include funds received directly from Federal agencies, through other State and local governments or other primary recipients. To assist recipients in identifying Federal funds, Federal agencies and primary recipients should provide the Catalog of Federal Domestic Assistance (CFDA) numbers to the institutions when making the awards.

(2) The review must include the selection and testing of a representative number of charges from each major Federal program. The selection and testing of transactions shall be based on the auditor's professional judgment considering such factors as the amount of expenditures for the program, the newness of the program or changes in its conditions; prior experience with the program, particularly as revealed in audits and other evaluations (e.g., inspections, program reviews or system reviews required by Federal Acquisition Regulation); the extent to which the program is carried out through subrecipients; the extent to which the program contracts for goods or services; the level to which the program is already subject to program reviews or other forms of independent oversight; the adequacy of the controls for ensuring compliance; the expectation of adherence or lack of adherence to the applicable laws and regulations; and the potential impact of adverse findings.

(a) In making the test of transactions, the auditor shall determine whether:

—The amounts reported as expenditures were for allowable services, and

—The records show that those who received services or benefits were eligible to receive them.

(b) In addition to transaction testing, the auditor shall determine whether:

—Matching requirements, levels of effort and earmarking limitations were met.

—Federal financial reports and claims for advances and reimbursements contain information that is supported by the books and records from which the basic financial statements have been prepared, and

—Amounts claimed or used for matching were determined in accordance with (1) OMB Circular A-21 "Cost principles for educational institutions"; (2) Attachment F of Circular A-110 "Uniform Requirements for Grants and Agreements with Institutions of Higher Education and other Nonprofit Organizations"; (3) Circular A-122 "Cost principles for nonprofit organizations"; and (4) FAR Subpart 31 cost principles.

(c) The principle compliance requirements of the largest Federal programs may be ascertained by referring to the *"Compliance Supplement for Single Audits of Educational Institutions and Other Nonprofit Organizations"*, and the *Compliance Supplement for Single Audits of State and Local Governments,"* issued by OMB and available from the Government Printing Office. For those programs not covered in the Compliance Supplement, the auditor may ascertain compliance requirements by researching the statutes, regulations, and agreements governing individual programs.

(3) Transactions related to awards that are selected in connection with examinations of financial statements and evaluations of internal controls shall be tested for compliance with Federal laws and regulations that apply to such transactions.

10. *Subrecipients.* Recipients that receive Federal awards and provide $25,000 or more of it in a fiscal year to a subrecipient shall:

a. Determine whether the subrecipients have met the audit requirements of this Circular.

b. Determine whether the subrecipient spent Federal funds in accordance with applicable laws and regulations. This may be accomplished by reviewing an audit of the subrecipient made in accordance with OMB Circulars, or through other means (e.g., program reviews) if the subrecipient has not yet had such an audit;

c. Ensure that appropriate corrective action is taken within six months after receipt of the audit report in instances of noncompliance with Federal laws and regulations;

d. Consider whether subrecipient audits necessitate adjustment of the recipient's own records; and

e. Require each subrecipient to permit independent auditors to have access to the records and financial statements as necessary to comply with this Circular.

11. *Relation to other audit requirements.* An audit made in accordance with this Circular shall be in lieu of any financial audits required under individual Federal awards. To the extent that a single audit provides Federal agencies with information and assurances they need to carry out their overall responsbilities, they shall rely upon and use such information. However, a Federal agency shall make any additional audits or reviews which are necessary to carry out its responsibilities under Federal law and regulation. Any additional Federal audits or reviews shall be planned and carried out in such a way as to avoid duplication.

a. The provisions of this Circular do not limit the authority of Federal agencies to make, or contract for audits and evaluations of Federal awards, nor do they limit the authority of any Federal agency Inspector General or other Federal audit official.

b. The provisions of this Circular do not authorize any institution or subrecipient thereof to constrain Federal agencies, in any manner, from carrying out additional audits, evaluations or reviews.

c. A Federal agency that makes or contracts for audits in addition to the audits made by recipients pursuant to this Circular shall, consistent with other applicable laws and regulations, arrange for funding the cost of such additional audits. Such additional audits or reviews include economy and efficiency audits, program results audits, and program evaluations.

12. *Cognizant agency responsibilities.* Cognizant Federal agencies will be assigned to oversee the implementation of this Circular.

a. The Office of Management and Budget will assign cognizant agencies for larger institutions. Other Federal agencies may participate with an assigned cognizant agency, in order to fulfill the cognizance responsibilities. Smaller institutions not assigned a cognizant agency will be under the general oversight of the Federal agency that provides them the most funds whether directly or indirectly.

b. A cognizant agency shall have the following responsibilities:

(1) Ensure that audits are made and reports are received in a timely manner and in accordance with the requirements of this Circular.

(2) Provide technical advice and liaison to institutions and independent auditors.

(3) Obtain or make quality control reviews of selected audits made by non-Federal audit organizations, and provide the results, when appropriate, to other interested organizations.

(4) Promptly inform other affected Federal agencies and appropriate Federal law enforcement officials of any reported illegal acts or irregularities. They should also inform State or local law enforcement and prosecuting authorities, if not advised by the recipient, of any violation of law within their jurisdiction.

(5) Advise the recipient of audits that have been found not to have met the requirements set forth in this Circular. In such instances, the recipient will be expected to work with the auditor to take corrective action. If corrective action is not taken, the cognizant agency shall notify the recipient and Federal awarding agencies of the facts and make recommendations for followup action. Major inadequacies or repetitive substandard performance of independent auditors shall be referred to appropriate professional bodies for disciplinary action.

(6) Coordinate, to the extent practicable, audits or reviews made by or for Federal agencies that are in addition to the audits made pursuant to this Circular; so that the additional audits or reviews build upon such audits.

(7) Oversee the resolution of audit findings that affect the programs of more than one agency.

13. *Illegal acts or irregularities.* If the auditor becomes aware of illegal acts or other irregularities, prompt notice shall be given to recipient management officials above the level of involvement. (See also paragraph 12c below for the auditor's reporting responsibilities.) The auditor shall also promptly report to proper Federal officials, including the audit officials and those entities of the illegal acts or irregularities and of proposed and actual actions, if any. Illegal acts and irregularities include such matters as conflicts of interest, falsification of records or reports, and misappropriation of funds or other assets.

14. *Audit Reports.* Audit reports must be prepared at the completion of the audit.

a. The audit report shall state that the audit was made in accordance with the provisions of this Circular. The report shall be made up of at least:

(1) The auditor's report on the financial statements and on a schedule of Federal assistance; the financial statements; and a schedule of Federal assistance. For recipients receiving 25 grants or more, the schedule of Federal assistance should contain changes in Federal award balances showing the total expenditures for federally assisted programs by funding agency and a schedule of changes in Federal award balances and a schedule of disbursements and expenditures for each student financial assistance program of the Department of Education. For recipients receiving less than 25 awards the schedule shall show the total expenditures for each award and program as identified in the *Catalog of Federal Domestic Assistance*. Federal programs that have not been assigned a catalog number shall be identified under the caption "other Federal assistance."

(2) The auditor's report on the study and evaluation of internal control structure. The report must identify the organization's significant internal accounting controls, or control structure including those controls designed to provide reasonable assurance that Federal programs are being managed in compliance with laws and regulations. It must also identify the controls that were evaluated, the controls that were not evaluated, the material weaknesses identified as a result of the evaluation and the scope of the auditor's work in obtaining an understanding of the internal control structure in assessing the control risk.

3. The auditor's report on compliance containing:

—An opinion as to whether major Federal programs were being administered in compliance with laws and regulations.

—A statement of positive assurance with respect to those items tested for compliance relative to the financial statements, including compliance with law and regulations pertaining to financial reports and claims for advances and reimbursements;

—Negative assurance on those items not tested;

—A summary of all instances of noncompliance including:

• The size of the universe in number of items and dollars.

• The number and dollar amount of transactions tested by the auditors.

• The number and corresponding dollar award in instances of noncompliance.

—An identification of total amounts questioned, if any, for each Federal award, as a result of noncompliance;

b. The three parts of the audit report may be bound into a single report, or presented at the same time or separate documents.

c. All fraud abuse, or illegal acts or indications of such acts, including all questioned costs found as the result of these acts that auditors become aware of, may be covered in a separate written report submitted in accordance with paragraph 14e.

d. In addition to the audit report, the recipient shall provide comments on the findings and recommendations in the report, including a plan for corrective action taken or planned and comments on the status of corrective action taken on prior findings. If corrective action is not necessary, a statement describing the reason it is not should accompany the audit report.

e. In accordance with Government Auditing Standards, reports shall be submitted by the auditor to the organization audited and to those requiring or arranging for the audit. In addition, the auditor shall submit copies of the reports to each Federal department or agency that provided Federal awards to the recipient. Subrecipient auditors shall submit copies to recipients that provided them Federal awards. The report shall be sent within 30 days after the completion of the audit, but no later than one year after the end of the audit period unless a longer period is agreed to with the cognizant agency.

f. Recipients of more than $100,000 in Federal awards shall submit one copy of the audit report within 30 days after issuance to a central clearinghouse to be designated by the Office of Management and Budget. The clearinghouse will keep completed audits on file.

g. Recipients shall keep audit reports on file for three years from their issuance.

15. *Audit Resolution.* As provided in paragraph 12, the cognizant agency shall be responsible for monitoring the resolution of audit findings that affect the programs of more than one Federal agency. Resolution of findings that relate to the programs of a single Federal agency will be the responsibility of the recipient and that agency. Alternate arrangements may be made on a case-by-case basis by agreement among the agencies concerned.

Resolution shall be made within six months after receipt of the report by the Federal departments and agencies. Corrective action should proceed as rapidly as possible.

16. *Audit workpapers and reports.* Workpapers and reports shall be retained for a minimum of three years from the date of the audit report, unless the auditor is notified in writing by the cognizant agency to extend the retention period. Audit workpapers shall be made available upon request to the cognizant agency or its designee or the General Accounting Office, at the completion of the audit.

17. *Audit Costs.* The cost of audits made in accordance with the provisions of this Circular are allowable charges to Federal awards.

a. The charges may be considered a direct cost or an allocated indirect cost, determined in accordance with the provisions of Circular A-21, "Cost principles for Universities" or Circular A-122 "Cost principles for nonprofit organizations," and FAR Subpart 31.

b. Generally, the percentage of costs charged to Federal awards for a single audit shall not exceed the percentage that Federal funds expended represent of total funds expended by the recipient during the fiscal year. The percentage may be exceeded, however, if appropriate documentation demonstrates higher actual cost.

18. *Sanctions.* No cost may be charged to Federal awards for audits that are not made in accordance with this Circular. In cases of continued inability or unwillingness to have a proper audit, Federal agencies must consider other appropriate sanctions including:

—Withholding a percentage of awards until the audit is completed satisfactorily;

—Withholding or disallowing overhead costs; or

—Suspending Federal awards until the audit is made.

19. *Auditor Selection.* In arranging for audit services institutions shall follow the procurement standards prescribed by Circular A-110, "Uniform Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and other Nonprofit Organizations."

20. *Small and Minority Audit Firms.* Small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals shall have the maximum practicable opportunity to participate in contracts awarded to fulfill the requirements of this Circular. Recipients of Federal awards shall take the following steps to further this goal:

a. Assure that small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals are used to the fullest extent practicable.

b. Make information on forthcoming opportunities available and arrange timeframes for the audit so as to encourage and facilitate participation by small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals.

d. Encourage contracting with small audit firms or audit firms owned and controlled by socially and economically disadvantaged individuals which have traditionally audited government programs and, in such cases where this is not possible, assure that these firms are given consideration for audit subcontracting opportunities.

e. Encourage contracting with consortiums of small audit firms as described in paragraph (a) above when a contract is too large for an individual small audit firm or audit firm owned and controlled by socially and economically disadvantaged individuals.

f. Use the services and assistance, as appropriate, of such organizations as the Small Business Administration in the solicitation and utilization of small audit firms or audit firms owned and controlled by socially and economically disadvantaged individuals.

21. *Effective date.* The provisions of this Circular are effective upon publication and shall apply to audits of nonprofit institutions for fiscal years that begin after January 1, 1989. Earlier implementation is encouraged. However, until this Circular is implemented the audit provisions of Attachment F to Circular A-110 shall continue to be observed.

22. *Policy Review (Sunset).* This Circular will have a policy review three years from the date of issuance.

23. *Inquiries.* Further information concerning this Circular may be obtained by contacting the Financial Management Division, Office of Management and Budget, Washington, DC 20503, telephone (202) 395-3993.

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